

Sapphire Foods

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Strong SSG performance in Q2; outlook remains encouraging

Sapphire's Q2 EBITDA was 3-7% lower than our estimates, owing to lower KFC margins. While KFC SSG at 15% was similar to DIL's at 13%, the PH SSG was relatively better at 23% vs. 3% for DIL. In our view, a higher dine-in focused store mix led to a better SSG performance for Sapphire. Store additions remained robust, with net adds of 42/79 stores in Q2/H1FY23, and Sapphire retained its outlook of doubling the no. of stores over the next 3-4 years. KFC's gross-margin decline of 310bps was higher than our expectations of 150bps, but operating leverage/cost cuts helped restrict the comparable brand margin decline to 80bps. While RM prices remain elevated (YoY), Sapphire expects to recoup brand margins with operating leverage. Encouragingly, Sapphire continued to deliver Rs100mn brand contribution from SL, despite the ~40% currency depreciation and high inflation in Q2. Capex/store in H1 reduced by ~16% YoY to Rs23mn, but was higher than the ~Rs14mn/store for DIL. We retain our EBITDA for FY24/25E, led by retention of near-term outlook. We expect Sapphire to deliver a strong EBITDA CAGR of ~45% over FY22-25E, led by a 21% store-count CAGR, 10% SSG, and gradual margin gains. Maintain BUY with TP of Rs1,650 (21x Sep-24 EBITDA).

Result summary: KFC's revenue grew by 36%, led by SSG (15%) and rest through new store adds. PH revenue gain was 60%, led by 23% gain in SSG with the balance via new store additions. Among channels, on-premise for KFC/PH saw faster growth, at 50-100% vs. 14-30% growth in the off-premise channel. With new menu launches, marketing initiatives and deeper penetration, Sapphire expects higher normalized SSG, at 8% for PH vs. 4-5% for KFC formats. Store additions at 42 remained robust, with 20/14 store additions for PH/KFC. Despite operating challenges, Sapphire added 8 stores in Sri Lanka (SL), highlighting its continued growth focus for SL. RM inflation led the 310/110bps decline in gross margin for KFC/PH formats in Q2. However, operating leverage helped restrict the comparable brand margin decline to 80bps for KFC, while PH brand margins saw a 440bps improvement on a low base. SL brand margins declined ~550bps, led by ~1,060 decline in gross margins.

Earnings-call KTAs: 1) Sapphire witnessed RM inflation in the mid-teen range, for which it took 9-10% price hikes in Apr-22. 2) SL's Q2 SSG of 37% in SLR terms was led by price hikes, while transaction growth was marginal. Operating conditions in SL are at ~85-90% of normalized levels. 2) While commodity prices remain elevated (YoY), Sapphire expects operating leverage to drive the QoQ improvement in EBITDA margin. 3) Based on historical trends, Sapphire anecdotally expects 4-8% improvement in KFC ADS for Q3 vs. Q2, while PH ADS is expected to remain similar due to lower seasonality. 4) Delivery mix via aggregator platforms is 90/80% for PH/KFC. 6) Sapphire does not expect to pay taxes in the near term due to accumulated losses.

Financial Snapshot (Consolidated)

(Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Revenue	10,196	17,216	23,587	30,815	38,885
EBITDA	1,244	3,050	4,615	6,272	7,985
EBITDA margin (%)	12.2	17.7	19.6	20.4	20.5
APAT	(999)	460	1,406	2,313	2,632
EPS (Rs)	(18.9)	7.2	22.1	36.4	41.4
EPS (% chg)	0.0	0.0	205.8	64.5	13.8
ROE (%)	(19.9)	6.2	13.0	18.3	17.4
P/E (x)	(76.9)	201.0	65.8	40.0	35.1
EV/EBITDA (x)	66.3	31.6	20.9	15.1	11.6
P/BV (x)	16.0	9.2	8.1	6.7	5.6

Source: Company, Emkay Research

CMP	Target Price
Rs 1,455	Rs 1,650 (■)
as of (November 3, 2022)	12 months
Rating	Upside
BUY (■)	13.4 %

Change in Estimates

EPS Chg FY23E/FY24E (%)	1/0
Target Price change (%)	-
Target Period (Months)	12
Previous Reco	BUY

Emkay vs Consensus

EPS Estimates		
	FY23E	FY24E
Emkay	22.1	36.4
Consensus	18.7	26.7
Mean Consensus TP (12M)	Rs 1,629	

Stock Details

Bloomberg Code	SAPPHIRE IN
Face Value (Rs)	10
Shares outstanding (mn)	64
52 Week H/L	1,574 / 909
M Cap (Rs bn/USD bn)	92 / 1.12
Daily Avg Volume (nos.)	1,63,036
Daily Avg Turnover (USD mn)	2.7

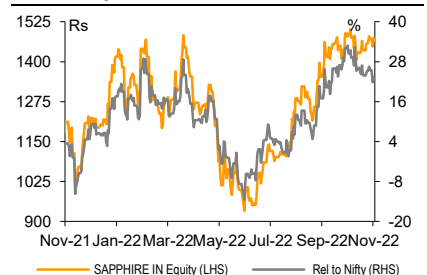
Shareholding Pattern [Quarter]

Promoters	51.3%
FIIIs	12.6%
DIIIs	15.6%
Public and Others	20.5%

Price Performance

(%)	1M	3M	6M	12M
Absolute	(2)	17	11	-
Rel. to Nifty	(8)	13	5	-

Relative price trend



Source: Bloomberg

This report is solely produced by Emkay Global. The following person(s) are responsible for the production of the recommendation:

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Exhibit 1: Performance across key metrics over the past few quarters

Key Metrics (Rs mn)	Q1FY22	Q2FY22**	Q3FY22**	Q4FY22	Q1FY23	Q2FY23
KFC India						
Number of stores	208	219	250	263	281	301
ADS ('000)	1,04,610	1,34,000	1,44,000	1,32,000	1,44,000	1,34,000
Revenue	1,788	2,565	3,031	2,966	3,537	3,491
Gross margin (%)	69.3	68.5	68.0	67.9	67.3	65.6
Brand contribution margin (%)	13.5	20.7	22.5	19.0	20.3	17.9
PH India						
Number of stores	171	188	209	219	235	249
ADS ('000)	48,720	53,515	64,000	55,000	61,000	64,000
Revenue	660	884	1,134	1,032	1,219	1,410
Gross margin (%)	76.5	75.8	75.4	74.8	75.3	74.7
Brand contribution margin (%)	5.8	16.2	17.3	11.5	14.8	15.1
Sri Lanka (Pizza Hut)						
Number of stores	69	73	89	95	98	106
ADS ('000)	92,030	1,05,000	1,21,000	1,12,000	75,000	73,000
Revenue	555	653	858	917	650	669
Gross margin (%)	66.9	66.2	67.2	64.9	58.8	55.4
Brand contribution margin (%)	18.0	21.5	26.4	24.4	15.5	15.0
Others (Maldives)						
Revenue	24	28	32	28	30	34
Brand contribution margin (%)	4.5	8.6	13.5	21.5	16.1	5.4
Sapphire - Consolidated						
Number of stores	450	482	550	579	616	658
Store additions	13	32	68	29	37	42
Revenue	3,027	4,130	5,055	4,943	5,436	5,604
Gross margin (%)	70.4	69.8	69.4	69.1	68.2	66.7
Brand contribution margin (%)	12.6	19.8	21.9	18.5	18.5	16.8
Overhead opex/revenue (%)	9.5	13.6	5.7	5.6	5.2	5.6
Consol. EBITDA	93	256	823	636	722	624
EBITDA margin (%)	3.1	6.2	16.3	12.9	13.3	11.1

Source: Company, Emkay Research; *EBITDA/margins are pre-IndAS-116, **PI note Q2/Q3FY22 brand margins across formats include one-off incentives from Yum Foods

Exhibit 2: Actual vs. Estimates (Q2FY23)

Rs mn	Actual	Estimates		Variation		Comment
		Emkay	Consensus	Emkay	Consensus	
Revenue	5,628	5,631	5,800	-0.1%	-3.0%	Revenues were in line with our estimates
EBITDA*	1,032	1,059	1,105	-2.5%	-6.6%	Higher margin decline in KFC led to lower margins
EBITDA margin* (%)	18.3%	18.8%	19.0%	-46	-71	
PAT	269	248	325	8.4%	-17.3%	PAT beat was largely due to higher other income and lower tax

Source: Company, Emkay Research; *EBITDA/Margins are post-IndAS-116 implementation

Exhibit 3: Quarterly performance (Consolidated)

Y/E, March (Rs mn)	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	YoY (%)	QoQ (%)	FY23TD	FY22TD	YoY (%)
Revenue	4,142	5,075	4,968	5,463	5,628	35.9	3.0	7,172	11,090	54.6
Expenditure	3,575	3,930	3,970	4,359	4,596	28.5	5.4	6,265	8,955	42.9
Consumption of RM	1,258	1,565	1,555	1,756	1,890	50.3	7.6	2,158	3,646	69.0
as % of sales	30.4%	30.8%	31.3%	32.1%	33.6%			30.1%	32.9%	
Employee Cost-Store	819	684	678	684	747	-8.7	9.3	1,378	1,431	3.8
as % of sales	19.8%	13.5%	13.7%	12.5%	13.3%			19.2%	12.9%	
Other expenditure	1,499	1,681	1,737	1,919	1,959	30.7	2.1	2,729	3,878	42.1
as % of sales	36.2%	33.1%	35.0%	35.1%	34.8%			38.0%	35.0%	
EBITDA	566	1,145	998	1,104	1,032	82.2	-6.5	907	2,136	135.5
Depreciation	512	513	576	609	628	22.7	3.1	1,045	1,238	18.4
EBIT	55	632	421	495	404	640.6	-18.4	-138	898	
Other Income	95	78	98	59	71	-24.7	21.1	204	130	-36.0
Interest	190	185	233	197	206	8.0	4.3	363	403	11.0
PBT	-41	525	286	356	269		-24.4	-297	626	
Total Tax	10	16	21	-25	1	-92.7		18	-24	
Adjusted PAT	-51	510	265	381	269		-29.6	-315	650	
Extra ordinary items	0	0	0	0	0			0	0	
Reported PAT before MI	-51	510	265	381	269		-29.6	-315	650	
Minority Interest	-1	0	0	-1	0			-1	-1	
Reported PAT	-50	510	265	383	269		-29.7	-314	652	
Reported EPS (Rs)	-1.0	8.0	4.2	6.0	4.2		-29.5	-6.0	10.2	

Margins (%)	2QFY22	3QFY22	4QFY22	1QFY23	2QFY23	(bps)	(bps)	FY23TD	FY22TD	(bps)
EBITDA	13.7	22.6	20.1	20.2	18.3	470	-190	12.6	19.3	660
EBIT	1.3	12.4	8.5	9.1	7.2	590	-190	-1.9	8.1	1,000
EBT	-1.0	10.4	5.8	6.5	4.8	580	-170	-4.1	5.6	980
PAT	-1.2	10.1	5.3	7.0	4.8	600	-220	-4.4	5.9	1,030
Effective Tax rate	-24.4	2.9	7.3	-7.1	0.3	2,470	730	-5.9	-3.9	200

Source: Company, Emkay Research; *EBITDA/Margins are post-IndAS-116 implementation

Exhibit 4: Peer comparison

Company	Price	M-Cap	Rating	TP	P/E (x)			EV/EBITDA (x)			EBITDA	EV/E-G (x)*
	(Rs)	(Rs bn)			FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	CAGR (%)	
Jubilant FoodWorks	608	401	Hold	595	70.2	56.0	45.2	41.3	33.6	27.8	21.7	1.9
Devyani International	183	221	Buy	225	77.3	63.4	48.3	43.5	33.1	26.4	28.3	1.5
Westlife Development	763	119	Buy	720	105.1	68.2	54.6	39.9	31.1	26.0	24.0	1.7
Sapphire Foods	1,455	92	Buy	1,650	65.8	40.0	35.1	30.7	21.1	16.1	38.0	0.8

Source: Company, Emkay Research; *EV/E-G is ratio of FY23E EV/EBITDA to FY23E-25E EBITDA CAGR expectations

Exhibit 5: Changes in estimates

Y/E, March (Rs mn)	FY23E			FY24E			FY25E		
	Earlier	Revised	% Change	Earlier	Revised	% Change	Earlier	Revised	% Change
Revenues	23,732	23,587	(0.6)	30,761	30,815	0.2	38,992	38,885	(0.3)
EBITDA*	4,713	4,615	(2.1)	6,252	6,272	0.3	7,986	7,985	(0.0)
EBITDA margin* (%)	19.9	19.6	-30 bps	20.3	20.4	0 bps	20.5	20.5	10 bps
PAT	1,395	1,406	0.8	2,313	2,313	(0.0)	2,647	2,632	(0.6)
EPS (Rs)	22.0	22.1	0.8	36.4	36.4	(0.0)	41.7	41.4	(0.6)

Source: Company, Emkay Research; *EBITDA/Margins are Post-IndAS-116 implementation

Exhibit 6: Sapphire – Growth construct of the business from the supply-side

Particulars	FY20	FY22	FY25E	FY35E	CAGR (%)	CAGR (%)
					FY25-35E	FY35+
KFC Stores (Sapphire)	187	263	451	1,052	8.8	2.5
PH Stores (Sapphire)	174	219	399	798	7.2	2.5
Others (SL/ Maldives)	66	97	123	233	6.6	2.5
Total Sapphire stores (no. of)	427	579	973	2,083	7.9	2.5
SSG (%)					6.5	5.0
Sapphire - Revenues (Rs bn)	13	17	39	156	14.9	7.6
EBITDA margins (%)	4.9	10.5	14.1	16.2		0.0
Sapphire - EBITDA	0.7	1.8	5.5	25	16.5	
Depreciation (% of EBITDA)	153.9	61.3	34.2	25.0		
Sapphire - EBIT	-0.4	0.7	3.6	19	18.0	7.6
EBIT margins (%)	(2.7)	4.0	9.3	12.1		

Source: Emkay Research, *EBITDA/Margins are Pre-IndAS-116 implementation

Exhibit 7: Sapphire – Target EV/EBITDA multiple derived from a two-stage dividend growth model

Particulars (Rs bn)	
Revenue CAGR [FY22E-25E] (%)	31
EBITDA CAGR [FY22E-25E] (%)	45
Net debt-to-EV (%)	-4
Stage-1: FY25E-35E	
EBITDA in Yr-0 [FY25E] (Rs)	5.5
EBITDA in Yr-1 (Rs bn)	6.5
EBITDA CAGR (%)	18.0
Years of growth [n]	10.0
Incremental RoIC (%)	63.0
WACC (%)	12.50
Tax rate (%)	25.2
Sustainable D&A-to-EBITDA (%)	25.0
Net debt to EV (%)	-4
Implied FCFF ratio (%)	71
Revenues in FY35E	204
Terminal stage	
Terminal EBITDA growth (%)	7.5
Incremental RoIC (%)	63.0
Implied FCFF ratio (%)	88.1
Fair value EV/EBITDA in Mar-25E (x)	19.0
EV in Mar-25E	123
Sep-23 NPV of FCFFs	3.2
Sep-23E EV	106
Adj. net debt	(4.0)
Fair value of Equity in Sep-23E (x)	110
Sep-24E EBITDA	4.8
Implied fair value EV/EBITDA in Sep-23E (x)	21.9
Premium applied to FV (%) [a]	-5.0
Target EV/EBITDA in Sep-23E (x)	21
Target market-cap in Sep-23E	105
Shares o/s (mn)	64
Target price in Sep-23E (Rs/share)	1,650

Source: Emkay Research; [a] Discount accounts for higher PE shareholding

Key Financials (Consolidated)**Income Statement**

Y/E Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Revenue	10,196	17,216	23,587	30,815	38,885
Expenditure	8,952	14,166	18,972	24,543	30,900
EBITDA	1,244	3,050	4,615	6,272	7,985
Depreciation	2,091	2,135	2,608	3,172	3,748
EBIT	(847)	915	2,008	3,100	4,236
Other Income	616	380	266	384	542
Interest expenses	756	781	853	1,050	1,260
PBT	(987)	514	1,420	2,434	3,518
Tax	12	54	14	122	887
Extraordinary Items	0	0	0	0	0
Minority Int./Income from Assoc.	0	0	0	0	0
Reported Net Income	(999)	460	1,406	2,313	2,632
Adjusted PAT	(999)	460	1,406	2,313	2,632

Balance Sheet

Y/E Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
Equity share capital	528	635	635	635	635
Reserves & surplus	4,271	9,436	10,842	13,155	15,786
Net worth	4,799	10,071	11,477	13,790	16,422
Minority Interest	(12)	(17)	(17)	(17)	(17)
Loan Funds	6,449	7,893	7,898	8,365	9,125
Net deferred tax liability	206	197	230	284	346
Total Liabilities	11,442	18,144	19,588	22,423	25,876
Net block	10,844	13,898	15,725	16,718	17,720
Investment	0	0	0	0	0
Current Assets	2,341	7,415	7,181	9,971	13,412
Cash & bank balance	768	4,071	4,047	6,045	8,672
Other Current Assets	0	0	0	0	0
Current liabilities & Provision	2,048	3,495	3,645	4,593	5,582
Net current assets	294	3,920	3,537	5,378	7,830
Misc. exp	0	0	0	0	0
Total Assets	11,442	18,144	19,588	22,423	25,876

Cash Flow

Y/E Mar (Rs mn)	FY21	FY22	FY23E	FY24E	FY25E
PBT (Ex-Other income) (NI+Dep)	(1,603)	134	1,154	2,050	2,977
Other Non-Cash items	0	0	0	0	0
Chg in working cap	23	(312)	379	196	219
Operating Cashflow	1,255	2,685	4,980	6,346	7,317
Capital expenditure	(826)	(2,672)	(2,935)	(2,665)	(2,750)
Free Cash Flow	429	13	2,045	3,681	4,567
Investments	0	0	0	0	0
Other Investing Cash Flow	0	0	0	0	0
Investing Cashflow	(210)	(2,292)	(2,669)	(2,281)	(2,208)
Equity Capital Raised	506	5,166	0	0	0
Loans Taken / (Repaid)	34	(164)	(599)	15	17
Dividend paid (incl tax)	0	0	0	0	0
Other Financing Cash Flow	(1,244)	(1,965)	(1,736)	(2,083)	(2,499)
Financing Cashflow	(824)	2,911	(2,335)	(2,068)	(2,482)
Net chg in cash	221	3,304	(24)	1,998	2,627
Opening cash position	547	768	4,071	4,047	6,045
Closing cash position	768	4,071	4,047	6,045	8,672

Source: Company, Emkay Research

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Key Ratios

Profitability (%)	FY21	FY22	FY23E	FY24E	FY25E
EBITDA Margin	12.2	17.7	19.6	20.4	20.5
EBIT Margin	(8.3)	5.3	8.5	10.1	10.9
Effective Tax Rate	(1.2)	10.5	1.0	5.0	25.2
Net Margin	(9.8)	2.7	6.0	7.5	6.8
ROCE	(2.0)	8.8	12.1	16.6	19.8
ROE	(19.9)	6.2	13.0	18.3	17.4
RoIC	(8.0)	6.8	13.7	18.8	19.2

Per Share Data (Rs)	FY21	FY22	FY23E	FY24E	FY25E
EPS	(18.9)	7.2	22.1	36.4	41.4
CEPS	20.7	40.8	63.2	86.3	100.4
BVPS	90.9	158.5	180.6	217.0	258.4
DPS	0.0	0.0	0.0	0.0	0.0

Valuations (x)	FY21	FY22	FY23E	FY24E	FY25E
PER	(76.9)	201.0	65.8	40.0	35.1
P/CEPS	70.3	35.6	23.0	16.9	14.5
P/BV	16.0	9.2	8.1	6.7	5.6
EV / Sales	8.1	5.6	4.1	3.1	2.4
EV / EBITDA	66.3	31.6	20.9	15.1	11.6
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0

Gearing Ratio (x)	FY21	FY22	FY23E	FY24E	FY25E
Net Debt/ Equity	1.2	0.4	0.3	0.2	0.0
Net Debt/EBITDA	4.6	1.3	0.8	0.4	0.1
Working Cap Cycle (days)	(17.0)	(3.2)	(7.9)	(7.9)	(7.9)

Growth (%)	FY21	FY22	FY23E	FY24E	FY25E
Revenue	(23.9)	68.8	37.0	30.6	26.2
EBITDA	(33.0)	145.2	51.3	35.9	27.3
EBIT	0.0	0.0	119.4	54.4	36.7
PAT	0.0	0.0	205.8	64.5	13.8

Quarterly (Rs mn)	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23
Revenue	4,142	5,075	4,968	5,463	5,628
EBITDA	566	1,145	998	1,104	1,032
EBITDA Margin (%)	13.7	22.6	20.1	20.2	18.3
PAT	(50)	510	265	383	269
EPS (Rs)	(0.9)	8.0	4.2	6.0	4.2

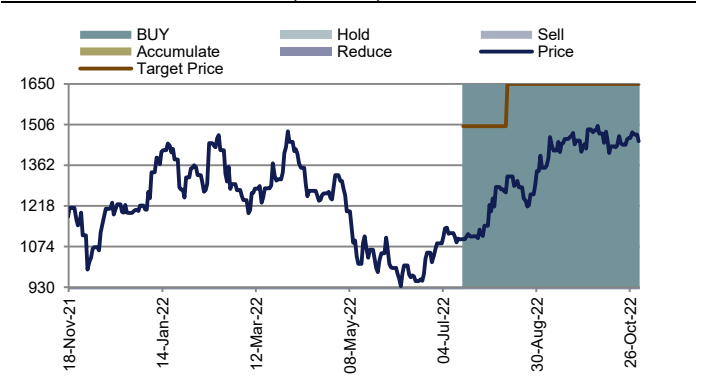
Source: Company, Emkay Research

RECOMMENDATION HISTORY (Rs/share)

Date	Closing Price	TP	Period	Rating	Analyst
21-Aug-22	1,284	1,650	12m	Buy	Devanshu Bansal
12-Aug-22	1,322	1,650	12m	Buy	Devanshu Bansal
16-Jul-22	1,101	1,500	12m	Buy	Devanshu Bansal

Source: Company, Emkay Research

RECOMMENDATION HISTORY (Rs/share)



Source: Bloomberg, Company, Emkay Research

Emkay Rating Distribution

Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

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Sources for all charts and tables are Emkay Research unless otherwise specified.

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